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IN THE

Supreme Court of the United States

October Term, 1935.

No. 29

RICHEY V. GRAHAM,
Petitioner,

v.

THE WHITE-PHILLIPS COMPANY, INC.,
Respondent.

CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

PETITIONER'S BRIEF.

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Petitioner.

Petition for Certiorari Filed April 23, 1935.
Certiorari Granted May 27, 1935.

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IN THE

Supreme Court of the United States

October Term, 1935.

No. 29

RICHEY V. GRAHAM,

Petitioner,

v.

THE WHITE-PHILLIPS COMPANY, INC.,

Respondent.

PENDING ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

The Petitioner, Richey V. Graham, on May 27, 1935, was, by this Honorable Court granted a writ of *certiorari* to the Circuit Court of Appeals for the Seventh Circuit to review the judgment entered by that Court on December 8, 1934 (R. 152) (rehearing denied on January 28, 1935, R. 153), reversing the decree of the District Court of the United States for the Southern District of Illinois, Southern Division, entered December 1, 1933 (R. 113-4), in favor of petitioner and against respondent, awarding

to the petitioner eight $1000 Illinois Highway Bonds theretofore stolen from his home in Cook County, Illinois, and subsequently purchased by the respondent, after the petitioner had given written notice by mail to the respondent of the said bonds having been stolen from his home.

The Petition for the writ of *certiorari* fully sets forth the facts in issue and the points assigned as error, as well as argument in support thereof.

The petitioner, desiring to amplify the reasons which he believes call for a reversal of the judgment of the Circuit Court of Appeals, now presents his Brief and Argument and submits the following for the consideration of the Court:

The Findings of Fact and Conclusions of Law (R. 105-110) were signed by Honorable Charles G. Briggle, Judge, and entered of record on December 1, 1933, without written opinion.

OPINION BELOW.

The opinion of the Circuit Court of Appeals (R. 144-152) is reported in *74 Fed. (2d) 417*.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered on December 8, 1934 (R. 152). Rehearing petition was filed on December 26, 1934 (R. 153), and denied on January 28, 1935 (R. 153). The jurisdiction of the Court is invoked under *Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 (Sec. 347-a, Title 28 U. S. Code). Certiorari* was granted May 27, 1935, upon a petition filed April 23, 1935.

QUESTIONS PRESENTED.

1. Whether, as a matter of law, The White Phillips Company, Inc., respondent, by reason of having actually received, prior to its purchase on September 22, 1930, of eight $1000 Illinois Highway Bonds from one J. A. Connolly, a notice that the same had been stolen from Richey V. Graham, failed to become a holder thereof in due course.

2. Whether the denial by the Supreme Court of the State of Illinois of a writ of *certiorari* upon the application of *Madison and Kedzie State Bank, Petitioner, v. Northwestern National Bank, Respondent,* to review and determine the judgment entered by the Appellate Court of Illinois, of the First District, did not under the holdings of said Supreme Court of Illinois, constitute an approval of the conclusion reached by the said Appellate Court of Illinois, First District, and whether the said action of the Supreme Court of Illinois, was not under its holdings, in effect, an affirmance of the judgment of the said Appellate Court in the cause of *Northwestern National Bank v. Madison & Kedzie State Bank,* reported in *242 Illinois Appellate Court Reports, at page 22.*

3. Does not, by reason of the denial of the said application for writ of *certiorari* by the Supreme Court of Illinois the conclusion reached by the Appellate Court of Illinois in *Northwestern National Bank v. Madison & Kedzie State Bank, 242 Ill. 22,* govern the decision of the Courts of the United States involving the same point with reference to causes of action arising within the State of Illinois, and hence is it not decisive of this cause now before the Court on writ of *certiorari?*

4. Whether, under the provisions of the *Illinois Negotiable Instruments Act*, the action of The White-Phillips Co., Inc., in adopting the policy of disregarding, ignoring and treating as "junk" all notices descriptive of bonds, securities or negotiable instruments that had been stolen, coming to it from the true owners thereof, so that no reference would be made to said notices at any time to ascertain whether or not the securities which the respondent was daily purchasing were listed on these notices as stolen, did not make the respondent guilty of bad faith in purchasing the bonds stolen from Richey V. Graham, inasmuch as the respondent prior to the purchase received printed notice of said bonds having been stolen, and gave no consideration to the information contained in said circular, but on the other hand wilfully disregarded it.

5. Whether the respondent The White-Phillips Co., Inc., did not at the time of the purchase of the bonds in question have knowledge of such facts that its action in taking such securities amounted to bad faith.

6. Whether the respondent has fully met the burden of proof requirement to the extent of establishing that none of its staff charged with responsibility of receiving notices, or buying bonds, had knowledge of petitioner Graham's ownership.

THE STATUTES INVOLVED.

The Statutes involved will be found in the Appendix, *infra*, pp. 36, 37.

STATEMENT.

THE FACTS. The petitioner, Graham, placed the 35 $1000 Illinois Highway bonds in a safe in his home. Burglars stole them on or about September 2, 1930. He immediately gave notice of the theft to the Foreman State Corporation and to others. Pursuant to its custom the Foreman Company mailed a report of this theft to a list of municipal bond dealers on or about September 5th. The Chicago branch of the respondent was on Foreman's mailing list.

Respondent is a dealer in municipal bonds with its principal office in Davenport, Iowa, and a branch office in Chicago.

Eight of the thirty-five stolen bonds were subsequently acquired by respondent from J. A. Connolly of St. Paul who, on September 13, 1930, wrote to the Chicago branch asking for bids on eight of these Illinois Highway bonds which had been stolen from Graham, giving the maturity dates. On the 16th, respondent's Chicago office wired a bid which was promptly accepted. Directions were given to ship the bonds to Davenport, but, accompanied by a sight draft payable to a Chicago bank, they were sent by Connolly to Chicago on September 22nd, and payment was promptly made by the Chicago office. The bonds were then sent to the Davenport office and received by it on September 23rd.

The case turns upon the matter of respondent's knowledge. It appears that when the bonds arrived in the Davenport office and were lying upon the desk of a clerk, that employee went to a pencil sharpener near by, and

while he was sharpening a pencil his eye chanced to fall upon the notice of a list of stolen bonds which hung upon a nearby wall hook. Observing that Illinois Highway bonds appeared thereon he recalled that such described bonds were on his desk. Upon examining the numbers of these bonds he discovered that they had been stolen. He notified the Chicago office which in turn tried to recover the purchase price from Connolly. Connolly was sent to jail where he died. No money was recovered, but the respondent immediately used the bonds as collateral to secure a loan from a Davenport bank.

There is evidence that both the Chicago and Davenport branches had in the past received notices of stolen bonds. It was the practice in the Chicago branch to place them in a drawer. The Davenport branch placed them on a hook. There were no directions to the employees as to the handling of them, and no settled policy was pursued in bringing such notices to the attention of the office; nor were tabulations or records kept of such lists; nor were they examined before bonds were purchased. No employee was instructed to note, record or circulate the contents of the lists.

In Davenport, the office boys in charge of the mail put the lists on the hook "because they didn't know of anywhere else to put them," and they also put other papers on the same hook.

(The foregoing is largely an abbreviation of the statement of facts by the Court of Appeals.)

The testimony of each witness called by respondent emphasizes so shockingly the lack of good faith toward the general public in the matter of guarding against buy-

ing stolen securities from thieves, and the contemptuous ignoring of all notices of stolen bonds being extant, that we quote liberally from the testimony in that regard.

It more than sustains the strong findings made by the Master in Chancery and the District Court that the purchase of the bonds in question was made in bad faith, and the findings of the Circuit Court of Appeals to the effect that there was no attention paid to printed notices that came in respondent's mail telling of the stealing of securities and warning against their purchase if presented.

This testimony follows:

Blair Phillips, President:

> Prior to the purchase of these bonds we never attempted to advise each office of such notices (R. 33).

Robert Alexander, Vice-President (Rec. 34-35):

> "There was not any custom or practice in our Davenport office of advising any member of the force of the receipt of notices of this character. If one of those mimeographed or printed notices came in the mail in our Davenport office, I don't know what became of it. There was no established method of handling. And I know of no instructions or orders in our office with respect to communicating with anybody in authority the fact of the receipt of notices of this character" (R. 35).

Carl Stutz, Secretary and bond buyer, in the Davenport office (R. 78-9-80):

> "There was nobody in the office whose business it was to refer to the information that had come in as to what was stolen."

Roy Crowe, stenographer employed by White-Phillips Company at Davenport:

"I have no recollection about the time that this paper came into the office.

"In the Davenport office if notices came in from various places that bonds had been stolen the notices were put on a clip on the glass around there. There was no custom or practice of circularizing that notice among the persons in the office, and there was no duty or custom on the part of anybody in the office of familiarizing themselves with these notices" (R. 39).

Vernon Ehlers:

* * *

"I have general supervision of the Davenport office. I handle all banking, all confirmations to customers, all correspondence with salesmen, etc., and those were my general duties in 1930" (R. 43).

"Sometimes there was consultation by wire, correspondence or otherwise between the Chicago office and the Davenport office in regard to the purchase of bonds before the purchase was effected, but this did not occur all the time" * * * (R. 44).

"The general and customary routine of the Davenport office with reference to the receipt of mail was that the first thing in the morning Mr. Offerman assisted by Mr. Drumm opened the mail" (R. 45). "It is my knowledge no instructions had been given to Offerman or Drumm or anyone else in the office with reference to stolen bond notices. If there had been any such instructions I think I would have known it. * * *

"There was no duty in the Davenport office with reference to anyone familiarizing himself or herself with the contents of that clip or hook. It was purely accidental that I detected this notice. * * *

"In the Davenport office there was no custom or routine with reference to the handling of stolen bond notices. * * *

"I could not say how many such notices came to our office, but every so often a notice of such type

would come through. Some of them would be ten or twelve legal-sized sheets in fine print listing bonds, numbers, coupons and all sorts of securities. I recall the list that was mailed out in connection with the robbery of a bank at Lincoln, Nebraska" (R. 46). "It was very voluminous. * * * On that clip the boys put any miscellaneous notices of any sort; most any ordinary junk that came into the office was hung on that hook. I have seen traffic posters and warnings—most anything might be on that hook. It was a clip for what junk came into the office and the boys opening the mail did not call it to the attention of anybody. Could not say how long it stayed there. I imagine when it got full it was taken off and destroyed. I simply saw this notice by accident because I happened to be sharpening a pencil" (R. 46).

"In the Chicago office they don't make a record of such notices, but they do file the list, I understand. They don't make a habit of checking over that list whenever they buy a bond. * * * It is possible to hire an employee to keep track of the notifications of bonds stolen and check that list before purchases are made." * * * (R. 47).

Ernest Bell, assistant secretary, in the Chicago office, paying and delivering bonds we bought (R. 49).

"We have received notices of securities having been stolen and those notices are in a nature of a warning not to purchase the stolen securities. All notices I ever received in the Chicago office covered bonds not dealt in by us and did not contain municipal bonds. I never received a notice with reference to municipal bonds. When notices came into our office we put them in the drawer with the other miscellaneous matter and disregards those notices. I have since ascertained that Connolly was convicted of transporting stolen bonds in the mail, and died in prison.

I know the Foreman State Corporation, but have never seen any notifications coming from the Foreman

> State Corporation with respect to stolen securities. Notices as to securities having been stolen would come in after they are sent out to us but not with great frequency; they would come very rarely and not at all on municipal bonds. I don't know any reason why notification would not come to our Chicago office of municipal bonds having been stolen" (R. 54).

Mr. Bell's entire testimony clearly shows he was a dishonestly inclined witness, seeking to adjust his testimony to the exigencies and perils of his employer's case. Furthermore, it does not appear that he was qualified to speak from his own actual knowledge, when he asserted that notices of thefts of municipals did not come to the Chicago office. The truth undoubtedly was that all notices were filed away without being first called to his attention.

Arno Schriefer, legal and office work, Chicago office:

> "The bonds were left with me, and a check given in payment. No attempt was made by looking up records or anything else to find out whether those bonds were stolen or have information at hand when the bonds should be presented to check up on them. We might have received notice that securities had been stolen. * * * When those bonds were presented, we did not make any effort to find out whether they were stolen when I purchased them, and I don't remember seeing Mr. Bell do it" (R. 40-1-2-3).

Master in Chancery Edward P. Allen found that copies of the notices entitled "Stolen Bonds" were mailed by the Foreman State Corporation to the White-Phillips Co. Inc., at its Chicago office and also the main office at Davenport (R. 87), and that the said The White-Phillips Co., Inc., received both of said notices entitled "Stolen Bonds", but that no examination was made of said notices, and no

consideration of the information as contained in said circular was given to it whatsoever, but on the other hand, totally and utterly disregarded (R. 88). He further found

> "that the policy of said The White-Phillips Co., Inc., in the handling of said notices received, either at the Chicago or Davenport offices of said Company, was of such a character that said notices were totally disregarded, and none of the clerks or office force of said Company were instructed to examine or refer to said notices of stolen securities; that the Executives of said Company considered all of said notices of like character as 'junk,' and that no system was followed in the handling of these notices, except in the Chicago office they were placed in a drawer with miscellaneous matters, and in the Davenport office were filed upon a clip, but no reference was made to them at any time to ascertain whether or not the securities which they were daily purchasing were listed on these notices as stolen (R. 88). The District Court found that no effort was at any time made by said respondent, either by consultation of the records in its office, or otherwise, to investigate or ascertain the title of said J. A. Connolly in and to said bond, or his right to dispose of the same, or to discover whether or not said bonds had been stolen (7th Fact finding p. 107); and (8th Fact finding) that the purpose of the hook or clip in the outer office at Davenport 'among other things was to hold and display notices of stolen securities of the character here involved; but that in said office no one of the employes, officers or agents of said respondent was charged with the duty of making any check upon the contents of such notices so received by said respondent, and no system for conveying or recording or preserving such information as might be contained in such notices and similar notices received at respondent's Chicago offices to the members of the office force of said respondent had ever been put into effect. That said hook or clip was used by the office boy who opened the mail, for the purpose

of holding a variety of circulars, notices as to stolen securities, which were not distributed by the office boy to individuals in the office for attention, and there was no policy or custom in said office requiring any one in the office to pay any attention to the said hook or clip or anything it held.' " (R. 107-8.) The Court's Tenth Fact finding is:

That the respondent, The White-Phillips Company, Inc., as a corporate entity, at and before it purchased the aforesaid bonds had, by virtue of the notice so received at its Davenport office, received actual notice that the same had been stolen from the said Richey V. Graham, the true owner thereof; that at the time of such purchase the said mimeograph notice was on the hook or clip hereinbefore referred to; that said notice was in such position that nothing more than a casual glance by a person standing in the vicinity thereof was required to convey information that the bonds here involved had been stolen; and that the failure and neglect of said respondent to observe and learn the contents of such notice prior to the purchase of the securities here involved must be considered as amounting to a wilful and conscious disregard of the rights of the true owners of said securities, the said Richey V. Graham (R. 108-9). The District Court's fifth and final conclusion of law is:

That the respondent, The White-Phillips Company, Inc., by reason of having actually received, prior to its purchase of the securities here involved, a notice that the same had been stolen as hereinabove set forth, did not, by the purchase of said bonds, become a holder thereof in due course, but that at such time the said respondent had knowledge of such facts that its action in taking such securities amounted to bad faith (R. 109-10).

In the decree the District Court adjudged:

> "That the exceptions filed by the respondent The White-Phillips Company, Inc., to the Report of Edward P. Allen, Master in Chancery, to whom this cause was hitherto referred, be and the same are hereby overruled" (R. 113).

The Court of Appeals in concluding its opinion held:

> "In determining this question, we assume that the notices which were sent out by the Foreman Company were received both at Davenport and Chicago; that there was a want of ordinary care upon the part of the Chicago branch in not making more elaborate provision for the dissemination of the knowledge which said notices gave; that in purchasing the bonds appellant paid full value therefor; and at the time it had no actual knowledge they were stolen; that it made no investigation to ascertain whether the said bonds were stolen other than to inquire as to the status of the party who offered them for sale; that the information which came from the receipt of such notice of the theft of eight Illinois Highway bonds had been forgotten" (R. 151).

SPECIFICATIONS OF ERRORS.

The Circuit Court of Appeals erred:

1. In holding that

> "the fact that the defeated party sought to review the decision and the Supreme Court of Illinois denied its application for a *certiorari* makes the decision in the case of *Northwestern National Bank v. Madison & Kedzie State Bank*, in the Appellate Court of Illinois, no more authoritative."

2. In holding that the rule announced in *Northwestern National Bank v. Madison and Kedzie State Bank, 242 Ill. App. 22*, had not been approved and passed on by the Supreme Court of Illinois by virtue of its having passed

on and denied application for a writ of *certiorari* to review said action of said Appellate Court in said cause.

3. In holding that the action of the highest Court of Illinois in approving the conclusion reached by the Appellate Court of Illinois in the case of *Northwestern National Bank v. Madison & Kedzie State Bank, 242 Ill. App. 22,* and the affirmance of said judgment by the Supreme Court of Illinois by reason of its denial of the application for a writ of *certiorari,* as aforesaid, did not govern the Courts of the United States with reference to the same point in the cause of action arising in the State of Illinois in favor of Richey V. Graham and against the White-Phillips Company, Inc., and brought to the District Court of the United States for the Southern District of Illinois, Southern Division, by removal from the Circuit Court of Sangamon County, Illinois.

4. In holding that the printed notice received by The White-Phillips Company, Inc., prior to its purchase of the eight Illinois Highway bonds for $1000 each, that the said bonds had been stolen from and were the property of Richey V. Graham, did not render the said purchase invalid and the said Company liable for the return to said Graham of said bonds as their owner.

5. In holding that the respondent when it purchased said bonds did not have actual knowledge of the infirmity or defect in the title to said bonds anl that the same were the property of Richey V. Graham.

6. In holding that the respondent, The White-Phillips Company, Inc., did not, when it acquired the eight Illinois Highway bonds from J. A. Connolly, have knowledge of such facts that its acts in taking the said bonds amounted to bad faith.

7. In reversing the decree and judgment of the District Court.

ARGUMENT.

I.

The denial by the Supreme Court of Illinois of a Petition for Writ of Certiorari to the Appellate Court of Illinois is an approval of the conclusion reached by the Appellate Court, and, in effect an affirmance of the judgment of such Court.

The decision below appears to be erroneous. We submit that when the Supreme Court of Illinois denied the application for a writ of *certiorari* in the case of *Northwestern National Bank v. Madison and Kedzie State Bank, 242 Ill. App. 22,* it thereby approved *the conclusion reached by the* Appellate Court and the denial of the said writ was in effect an affirmance of the judgment of the Appellate Court. The Supreme Court of Illinois so ruled in the case of *Soden v. Claney, 269 Ill. 98-102,* and a close reading of *People v. Grant, 283 Ill. 391, 397,* shows that the Court still adheres to its ruling in *Soden v. Claney, supra,* as it points out that the case under consideration presented a different case than the one counsel had referred to that had been before the Appellate Court where the Court had denied a writ of *certiorari.*

The Court says in the *Grant case* that the denial of the writ of *certiorari* in the mandamus case therein referred to meant nothing more than "that we approve the conclusion of the Appellate Court that the State's Attorney should have signed and presented the petition".

This Court adopted the ruling of the Illinois State Supreme Court that the denial of a writ of *certiorari* is

an approval of the conclusion reached by the Appellate Court and in effect is an affirmance of the Appellate Court judgment, in the case of *Minneapolis, St. Paul and Sault Ste. Marie Ry. Co., Petitioner, v. John Rock, 279 U. S. 410 (412),* and cited *Soden v. Claney, supra,* and *People ex rel. Hoyne v. Grant, supra,* as establishing that rule of the Illinois Supreme Court. In the same case this Court holds that:

> "Whenever the highest Court of a state by any form of decision *affirms* or denies *the validity of a judgment of an inferior Court,* over which it can by law exercise Appellate authority, the jurisdiction of this Court to review such decision, if it involves a Federal question, will, upon a proper decision, attach."
> *Petitioner v. Rock, supra.*

The Supreme Court of Illinois having in the case of *Soden v. Claney, supra,* definitely ruled that its denial of a writ of *certiorari* to the Appellate Court is an approval by the same Supreme Court of the conclusion reached by the Appellate Court in the case before it, and therefore obviously an affirmance of the judgment, and this honorable Supreme Court of the United States having ruled that, so far as Illinois is concerned, a denial of the writ of *certiorari* to the Illinois Appellate Court is an approval of the conclusion reached by the Appellate Court and in effect an affirmance of its judgment, we cannot accept the respondent's *ipsi dixit,* on page 14 of its brief in opposition to our petition for the writ of *certiorari,* that the affirmance of the Appellate Court judgment in *Northwestern National Bank v. Madison & Kedzie State Bank, supra,* (by way of denial of the *certiorari* writ) was not a construction of the *Negotiable Instruments Act* by the highest Court of our State.

Respondent blows hot and cold when it denies the foregoing proposition, but admits that the writ "denial was

an affirmance of the judgment". Respondent sets up a bogey man in asserting that we contend that the denial of the writ was "An adoption of the reasoning and expression of the Appellate Court." For the purpose of the argument before this Honorable Court, it is immaterial to us what the reasoning and expressions contained in the opinion of the Appellate Court of Illinois are, so long as it is incontrovertible that the sole question presented to the Appellate Court was whether receipt of a list of securities alleged to have been stolen constitutes "actual knowledge" within the meaning of *Section 56 of the Negotiable Instruments Act, at a subsequent date,* of an infirmity or defect in the title of the person then negotiating some of said securities.

Both the losing party applying for the writ and the Appellate Court were in agreement that that was the question involved, and the respondent here has not yet had the temerity to claim that that is not correct. Therefore it surely follows that the Supreme Court of Illinois ruled in *Northwestern National Bank v. Madison & Kedzie State Bank, supra,*

(a) We adopt the conclusion of the Appellate Court; and

(b) We affirm the judgment of the Appellate Court; and consequently

(c) We deny a writ of *certiorari.*

We make bold to assert, therefore, that:

II.

The conclusion reached by the Appellate Court of Illinois in Northwestern Bank v. Madison & Kedzie State Bank, was adopted by the Supreme Court of Illinois when it denied the Petition for a Writ of Certiorari and affirmed the judgment of the Appellate Court; and that holding, therefore, is decisive of the instant case.

Northwestern National Bank v. Madison & Kedzie State Bank, supra.

III.

It is the holding of the highest State Court of Illinois, that one who purchases a security after he has received notice of infirmity in the instrument, or defect in the title of the person negotiating it, is not a holder in due course.

The Supreme Court of Illinois has uniformly held that notice of a defect in the title to an otherwise negotiable instrument, if previously served upon the party purchasing makes him *not* a holder in due course.

Northwestern National Bank v. Madison & Kedzie State Bank, supra.

(Writ of *certiorari* denied by the Supreme Court, *242 Ill. App. XIV.)*

This is so, because the *Illinois Negotiable Instruments Act* in its several sections uniformly declares that when notice is given of an infirmity in an instrument or of a defect in the title of a holder, the person receiving the notice ceases from the time of receiving of the notice to be a *bona fide* holder of any values to the holder of the instruments not theretofore extinguished by payment or otherwise theretofore satisfied.

Thus by *Section 52* a holder in due course is defined (2) as one who became the holder *"without notice"* that it has been previously dishonored, and (4):

> "that at the time it was negotiated to him he had no *notice* of any infirmity in the instrument or defect in the title of the person negotiating it."

Here are two provisions in one section of the statute that provide that *notice* of a defect in an instrument or in

the holder's title is all that is required to protect the rights of the party complaining and on whose behalf the *notice* has been given. No equivocation or special limited meaning of the word *notice* can be read into this section. It cannot be contended that in addition to *notice* lasting knowledge and memory must be ever present and follow the giving of the *notice.*

(We claim it is obvious that the word "had", as used in *Section 52,* relates to a past event, and that the word "have" is descriptive of present possession, while "must have had" in *Section 56* surely refers to a past or previous acquisition of knowledge or notice.

In other words, had is the past participle of have. Any uncertainty as to the meaning of "had" as used in *Section 52* is clarified by the words "must have been" used in *Section 56.*

The instant case that is before the Court on *certiorari* is certainly one that the Illinois Statute was designed to cover. When the $8000 of bonds were bought from the felon, Connolly, the respondent *had* a printed notice impaled on a hook on its cashier's desk in its main office in Davenport to the effect that those Illinois Highway bonds had been stolen from petitioner Graham. It had also received a similar notice at its Chicago office, but owing to its custom of keeping no track or record of notices so received, some of its employes testified that they knew nothing of such a record. The notice was not ambiguous, and its receipt is admitted, therefore, it "*must have* had actual knowledge of the defect of title".)

Section 54 likewise provides that the receiving of *notice* before the payment of the full amount agreed to be paid therefor makes the receiver person "a holder in due course only to the extent of the amount theretofore paid by him."

Section 56 provides that the notice of infirmity in an instrument or of defect of time must be such *notice* as will be brought home to the party with whom the instrument is negotiated.

Many persons prepare, publish and send out notices of loss by theft, or otherwise, of negotiable instruments belonging to them, and the notice is usually given wide circulation. But unless the notice is proved to have been *received* by the party charged, it is insufficient to defeat the purchaser's holder's title. Therefore the legislature wisely provided in *section 56* that the party to be charged *"must have had actual knowledge of the infirmity or defect."*

This means two things, *i. e.*, (1) the *notice* in its language must be sufficient to bring home *knowledge* to one reading it; and (2) the *notice* that definitely conveys *knowledge* must have been served and *received* by the party.

But real *Notice*—a served *notice*, that by its language conveys the necessary information to the one served is all the *actual knowledge* that the statute requires.

Where a *notice* meeting these requirements has been received by one negotiating for an instrument, he thereafter buys or acquires the instrument at his peril.

This is so held in *Northwestern National Bank v. Madison & Kedzie State Bank, supra, Certiorari* denied by the Illinois Supreme Court, *242 Ill. App. XIV.*

First State Bank v. First Nat. Bank, 314 Ill. 269, 273.

It will be noted that the Court in the last mentioned case uses the word "apprised", in quoting from and construing *Section 54 of the Negotiable Instruments Act.*

To the same effect, *Foncannon v. Lewis, 327 Ill. 455, 461.*

In *Renfrow v. Kramer, 341 Ill. 398, at 406,* it is held:

> *"Sections 52 and 56 of the Negotiable Instruments Act* define a holder in due course. Among other conditions the statute requires that at the time the holder took the paper he had no *notice* of any infirmity in the instrument or defect in the title of the person negotiating it. By *Section 56* of that act it is provided that where one has actual knowledge of any infirmity in the instrument or defect in the title of the one transferring it, or knowledge of such facts as to render his act in taking the instrument one of bad faith, such person is not a holder in due course."

Here again the Supreme Court of Illinois has adhered to the proposition that it is the matter of "notice" that governs the question as to whether a person is a holder, or not, in due course. Seemingly the Court sets up three classifications which disbar a person from being a holder in due course, the first classification being where he has had notice of infirmity or defect. That means a direct communication to him setting forth that the securities which he may later on want to accept, are defective or held by somebody whose title is spurious.

The second classification that the Supreme Court of Illinois undoubtedly evolves from the *Negotiable Instruments Act* is one where regardless of whether or not notice has been given, the recipient has actual knowledge of infirmity in the instrument, or defect in the title.

A third classification made by the Court is one where the recipient has knowledge of such facts as to render his act in taking the instrument one of bad faith.

We call special attention to the wording of the opinion in *Renfrow v. Kramer*, just cited, where it says:

> "Among other conditions the statute requires that at the time the holder took the paper *he had no* notice of any infirmity of the instrument or defect in the title of the person negotiating it."

How can the language of the Statute, and the wording of the foregoing opinion as well, be so distorted as to make it appear that on September 22, 1932, the White-Phillips Company had no notice of the theft of the bonds, when the proof shows, and the respondent admits, that it did have such notice theretofore, to-wit, on September 6, 1932, being the notice mailed by the Foreman Bank Corporation at Chicago on September 4th?

The conclusion reached by the Illinois Appellate Court in *Northwestern National Bank v. Madison & Kedzie State Bank, supra*, was that:

> "As a matter of law receipt by a bank on the 5th day of January, 1925, of a circular list of securities alleged to have been stolen from a bank in a sister state constitutes 'actual knowledge' within the meaning of *Section 56 of the Uniform Negotiable Instruments Act*, at a subsequent date, viz., May 9, 1925, of an infirmity or defect in the title of the person then negotiating some of such securities."

The foregoing interpretation of the ruling of the Appellate Court was submitted to the State Supreme Court by the Madison and Kedzie State Bank, the petitioner for the writ, with the statement that "the judgment of the Appellate Court was based solely upon its (that) ruling," and that:

> "The precise point is exceedingly important to the banking and commercial industries of Illinois, in fact to the public at large. It has never been ruled on by this (Ill. State Supreme) Court, or as far as we can determine by any other court in construing the Uniform Negotiable Instruments Act."

See copy of petition for writ of *certiorari* (R. 142, with certificate of Adam F. Bloch, Clerk of said Illinois Court).

And the Appellate Court of Illinois likewise defines the question involved and the conclusion reached in its decision when it sets forth in its opinion:

> "The real question, as we conceive it, is whether on the undisputed fact defendant received said notice in the manner aforesaid, it is chargeable with the actual knowledge of the theft when it received the bonds" (R. 138). * * * "The notice having been received by the proper agent of the bank to receive, open and acknowledge its mail in the line of his duties, we think the bank is estopped from claiming that it did not have actual knowledge of the effect of the bonds it subsequently received. * * * In this view of the case we think upon the undisputed evidence defendant had actual knowledge that the bonds were stolen, and as a matter of law, therefore, was not a holder in due course under the *Uniform Negotiable Instruments Law*. Accordingly, as a matter of law the judgment will be reversed" (R. 139-140).

The notice was undoubtedly received at Davenport on September 6th, and it was placed on the clip at the cashier's cage when the employe of the respondent opened the mail. This we have positive evidence of inasmuch as there is direct testimony of the notice having been mailed on the 4th to both the Chicago and the Davenport offices, and direct testimony of its subsequent finding at the cashier's cage at Davenport.

Therefore, it follows that the respondent had the notice on the 6th, and on every day thereafter up to and subsequent to the time it purchased the bonds from Connolly. In fact it *had* the notice in its files on the 16th of September, when it gave Connolly a quotation on the High-

way bonds that proved when presented to the respondent six days later to be the identical bonds that had been stolen from petitioner. The only reason that we cannot positively assert that the respondent *had* the same notice in its Chicago office every single day from September 5th on is because it was given no attention when received in the mail. No occupant in that Chicago office has denied that it was received, and the Courts have found that it was in fact received. Therefore, we emphasize these facts that:

A. THE RESPONDENT HAD THE NOTICE EACH DAY FROM SEPTEMBER 5TH TO 22ND, ON THE CLIP AT ITS CASHIER'S CAGE; and

B. *Renfrow v. Kramer, supra,* holds that the Statute requires that AT THE TIME THE HOLDER TOOK THE PAPER HE HAD NO NOTICE OF ANY * * * DEFECT IN THE TITLE OF THE PERSON NEGOTIATING IT;

C. *Section 52 of the Illinois' Negotiable Instruments Act* defines a holder in due course as:

"A holder who has taken the instrument under the following conditions: * * *

4. THAT AT THE TIME IT WAS NEGOTIATED TO HIM HE HAD NO NOTICE OF ANY INFIRMITY IN THE INSTRUMENT OR DEFECT IN THE TITLE OF THE PERSON NEGOTIATING IT."

What an absurdity it would be to have a statute passed worded similarly to the foregoing paragraph, but with the added qualification,

"unless the person shall have forgotten that he had and still has the notice of defect in his possession, or unless the person shall have purposely ignored and destroyed the notice which he received, in either of which events he will be deemed to be a holder in due course".

What constitutes notice where the term is used in various statutes of Illinois, or is otherwise a requirement of law, is defined in the following Illinois decisions:

Seaverns v. Presbyterian Hospital, 173 Ill. 414, 420.

Simmons v. Roseland Security Vault Co., 331 Ill. 563-574.

Drouineau v. Bank, 244 Ill. App. 251.

First National Bank, Taylorville, v. Kalb, 256 Ill. App. 159.

Peru State Bank v. Waggett, 230 Ill. App. 522.

Tollifsen v. Midle States Inv. Co., 253 Ill. App. 320.

Housh v. Tolson, 254 Ill. App. 126-132-134.

Metcalf v. Draper, 98 Ill. App. 399-404.

So that it seems a certainty:

(1) That the Illinois Legislature made the serving of notice of the infirmity or defect of title to a negotiable instrument complete protection to the true owner of the instrument, against a subsequent purchaser of stolen securities who had therefore received a copy of the notice.

(2) The Supreme Court of Illinois has repeatedly defined what method of service of notice is sufficient to bind a corporation; and

(3) When the Appellate Court in the case of *Northwestern National Bank v. Madison & Kedzie State Bank, supra*, followed the wording of the Statute and the holdings of the Supreme Court as to the binding effect of notice properly served, the Illinois Supreme Court adopted the conclusion of the Appellate Court and chose to in effect affirm the judgment rather than unnecessarily in-

crease its labors by enlarging its hearing docket, especially as it had in other cases herein cited adopted the wording of the Statute as setting forth the law of negotiable instruments in Illinois.

IV.

It is now the settled law that the provisions of the Negotiable Instruments Act of Illinois are to be accepted by all Federal Courts as interpreted by the Supreme Court of Illinois.

Burns Mortgage Company v. Fried, 292 U. S. 487.

V.

The Circuit Court of Appeals erred in not accepting the construction given to the Negotiable Instruments Act by the Supreme Court of Illinois.

If we are correct in the foregoing propositions, it follows that the holding in *Northwestern National Bank v. Madison & Kedzie State Bank, supra,* was binding on the District and Circuit Court of Appeal Courts in the instant cause and that the District Court followed the law as to notice as declared by the State Courts of Illinois, while the Circuit Court of Appeals in not following the rulings of the State Courts committed error in their reversal of the decree of the District Court.

Moreover, we believe that the Circuit Court of Appeals overlooked its ruling in *C. F. Childs & Co. v. Harris Trust & Savings Bank, 27 Fed. (2nd) 633,* decided in the year 1925, where the holding was first, that the rights of a party taking negotiable instruments in Illinois would be

determined according to the laws of this State, and second, that the receipt of the *notice* of the character here involved would prevent the recipient thereof from thereafter becoming a holder in due course.

We further submit that the Court failed to distinguish the case of *Merchants National Bank v. Detroit Trust Company, 258 Mich. 526,* from the instant "bad faith" case, in that in the Michigan case it was clearly proven that the treatment of the bank of notices received in the mail to the effect that securities had been stolen showed an honest purpose on the part of the bank of avoiding if possible the purchase of securities in all cases where notices had been given it and received through the mail, or otherwise, of theft having occurred.

Furthermore, the receipt of the notice of theft was denied and the denial was followed by proof that the Bank did not receive the notice. This, the Court held, rebutted the *prima facie* presumption that arises from testimony as to the mailing of the notice, and the defense's evidence in that regard was not met. So that a sufficient answer to the reference to this case is that the fact defense was sustained, and the reversal on appeal was because the plaintiff did not prove its case.

The Circuit Court of Appeals also erred in holding that the information which came from the receipt of notice of the theft *had been forgotten.* As no employee but the office boy who hung the notice on the hook had knowledge of its contents, and certainly the person conducting the purchase had no such knowledge, there was nothing to forget. If the notice in itself was not sufficient to disqualify the ownership of the respondent, then we submit that the knowledge by the respondent that such notices that came

to its offices advising it of bonds and securities with certain serial numbers having been stolen from the rightful owner, and warning the respondent not to purchase the same, were never called to the attention of the employes of the respondent and never given any consideration, and never served as a deterent to the purchase of such securities, constituted knowledge of such facts that respondent's action in acquiring instruments which it had been definitely advised were stolen instruments, amounted to bad faith towards the public and towards the true owners of such securities.

VI.

Under the facts as found by the Master, and by both the District Court and the Circuit Court of Appeals, the respondent was, as a matter of law, guilty of bad faith in acquiring the eight highway bonds, and liable to the petitioner, Graham, therefor.

The facts having been established in the District Court that the respondent received printed notices by mail in both its offices, notifying it that $35,000 of Illinois Highway bonds had been stolen from the residence of petitioner, and that no examination was made of said notices, and no consideration whatsoever was given of the information contained in said circular, but on the other hand, the same was totally and utterly disregarded (R. 88); and that the policy of the White-Phillips Co., Inc., was to disregard all notices of stolen securities and to consider them as "junk" and to make no reference to them at any time to ascertain whether or not the securities which they were daily purchasing were listed on these notices as stolen (R. 87-88), and that within less than eleven days after the said notices had been received by the respondent it

offered to, and six days later did, purchase eight of the stolen bonds from J. A. Connolly, a non-resident stranger; and that no effort was at any time made by said respondent (W-P Co.), either by consulting the records of its office, or otherwise, to investigate or ascertain the title of Connolly in and to said bonds, or his right to dispose of the same, or to discover whether or not said bonds had been stolen (R. 107), established as a matter of law that the respondent under the provisions of *Sections 52, 54 and 56 of the Illinois Negotiable Instruments Law* was not a holder in due course of the eight bonds in good faith; and that at the time of the negotiation it had received

> "*Notice of an infirmity in the instrument or* (and) *defect in the title of the person negotiating the same, and the respondent had actual knowledge of the infirmity or defect* (in that it had received the circular notification of the bonds having beeen stolen), *and knowledge of such facts* (to wit: its policy of disregarding such and all other like warnings) *that its action in taking the instrument amounted to bad faith.*"

The words in italics are the words used in *Section 56 of the Illinois Negotiable Instruments Act.*

And the Master in Chancery in his report, and the District Court in its Findings of Fact and Conclusions of Law, both so found.

The wording of *Section 56 of the Illinois Statute* defining "What is notice of defect" is in the past tense, *i. e.*, "the person to whom it is negotiated must *have had* actual knowledge of the infirmity or defect," and we submit that the language and effect of the statute cannot be evaded by showing that the party receiving the instru-

ment *had had* knowledge of the defect in the instrument he subsequently purchased, but that as a matter of business policy he cast aside and ignored the notice.

The Supreme Court of Illinois has directly construed the *Negotiable Instruments Act* and the bad faith rule.

In *Renfrow v. Kramer, supra,* it is held:

> "If circumstances are shown in evidence which by their fair and reasonable inferences tend to show bad faith as defined in the *Negotiable Instruments Act.* the question whether the plaintiff is a holder in due course becomes one of fact for determination by the jury. *(Foncannon v. Lewis, 327 Ill. 455.)* In this case there is not only evidence of want of consideration and fraud practiced against the Kramers, but there is also evidence of knowledge on the part of Renfrow at least of such want of consideration."

To the same effect, see *Bell v. McDonald, 308 Ill. 329, 335.*

VII.

The Bad Faith Rule.

The bad faith doctrine, grudgingly recognized decades ago, is properly given broader interpretations in these days, obviously as a matter of public policy which demands cooperation from the business interests, in hampering high powered gangsters in the disposal of the proceeds of their spectacular burglaries and robberies.

The Federal Courts have sustained this "bad faith" doctrine which existed under the common law, and is a part of the uniform *Negotiable Instruments Act,* and the State Courts have also.

We cite the holdings in *Goodman v. Simmonds, 20 How. 343, 367,*

"gross negligence may be evidence of *mala fides*"; *Murray v. Lardner, 69 U. S. 110, 121,* "The rule may perhaps be said to resolve itself into a question of honesty or dishonesty, for guilty knowledge and wilful ignorance alike involve bad faith. They are the same in effect; *Vermilye v. Adams Express Co., 21 Wall. 138, 146,* 'Bankers and brokers cannot, more than others, when warned of possible or probable danger in their business, shut their eyes and plead a want of knowledge which is wilful;' *Hotchkiss v. National Shoe & Leather Bank, 21 Wall. 354, 359.* 'Bad faith which implies guilty knowledge or wilful ignorance'"

on the part of the purchaser must appear.

The case of *Morris v. Muir, 111 Misc. (N. Y.) 739,* where the practice of the brokers in so conducting their office that people could apply there and without question being raised dispose of their securities whether stolen or otherwise, correctly states the bad faith rule. This case was affirmed in the Appellate Division on the opinion below. Therein many cases are cited to sustain its finding of bad faith in the case reviewed. Thus:

"The manner in which the defendants conducted their Liberty loan department provided an easy way for thieves to dispose of their plunder. It is a case of 'no question asked'. I do not for one moment wish to charge the defendants with the intention of extending an invitation to bond thefts. They are men of good reputation. I believe it is only necessary to call their attention to the lack of precautionary measures and that the proper remedy will be applied.

"Upon the facts in this case I do not hesitate in arriving at the conclusion that the action of the defendants in buying the bonds amounted to bad faith

within the authorities. The defendants were grossly negligent in purchasing the bonds. Although gross negligence does not of itself constitute bad faith as a matter of law, it is evidence from which bad faith may be inferred. *Bipp v. Smith, 137 Wis. 234.*"

"The term 'bad faith' as used in the Statute does not necessarily involve furtive motives *(Ward v. City Trust Co., 192 N. Y. 61, 73);* it means bad faith in a commercial sense. *Rochester & Charlotte Turnpike Road Company v. Paviour, 164 N. Y. 281, 286.*"

In the latter case, at page *284*, the Court says:

"While he was not bound to be on the watch for facts which would put a very cautious man on his guard, he was bound to act in good faith. *(Second National Bank v. Weston, 161 N. Y. 520, 526; Cheever v. Pittsburgh, etc. R. R. Co., 150 N. Y. 59, 66.)* Even if his actual good faith is not questioned, if the facts known to him should have led him to inquire, and by inquiry he would have discovered the real situation, in a commercial sense he acted in bad faith and the law will withhold from him the protection that it would otherwise extend."

Wilful disregard of known facts showing want of title *or wilful evasion of knowledge of the facts amounts to bad faith. Matter of Hopper-Morgan Co., 156 Fed. Repr. 525.*

In *Hallock v. Young, 72 N. H. 416, 419, 420; 57 Atl. 236, 238,* the Court said:

"It was said in the leading case on the subject in this country, that 'while he is not obliged to make inquiries, he must not wilfully shut his eyes to the means of knowledge which he knows are at hand • • • for the reason that such conduct, whether equivalent to notice or not, would be plenary evidence of bad faith.'"

VIII.

The Burden of Proof.

The proof is overwhelming that nobody connected with the respondent made it his business to make note of warnings that securities had been stolen and should not be purchased. But the defendant sought to prove good faith by calling certain of its employes and proving by them that they, said witnesses, had not seen the notices that had been sent to the firm notifying it that the Highway bonds in question had been stolen from the petitioner.

This leads to a discussion of the doctrine of the Burden of Proof. Respondent has heretofore conceded that the burden was upon it to establish good faith. This is so by reason of *Section 59 of the Illinois Negotiable Instruments law (Par. 79, Chap. 98. Cahill's Illinois Statutes—1933)*, which is in part as follows:—

> "Every holder is deemed *prima facie* to be a holder in due course; but when it (is) shown that the title of any person who has negotiated the instrument was defective, the burden is on the holder to prove that he or some person under whom he claims acquired the title as a holder in due course."
>
> *Security v. American Trust & Savings Bank, 162 Ill. App. 76.*

And it did not meet that burden. As already indicated, in September of 1930 it had 27 officers and employees in the Davenport office, and 5 or 6 in the Chicago office. But out of all that number it called but 11 witnesses to testify to its want of knowledge of the rights of the true owner at the time of the purchase of the bonds in suit. Aside from its President it called 6 from the Davenport

office, and 4 from the Chicago office. Where were the others of its officers and employees? There was no evidence that the ones called were the only persons connected with respondent who had authority to receive notices of stolen bonds, or to buy bonds, or even that it had called all those who had to do with this particular purchase. How then can respondent now be heard to say that it successfully carried the burden of showing its good faith as regards this transaction? It had the facilities to protect the rights of the true owner of these bonds. It had installed a device for the receipt of notices of stolen bonds, and had received a printed notice of the theft of the particular bonds here involved. For at least ten days prior to the purchase that notice in bold characters hung upon the wall in the Davenport office at the very place provided for notices of that kind. There is absolutely no evidence that such notice had not been read and its contents duly noted and learned, by at least 21 of the officers and employees working in and out of the Davenport office, including persons duly authorized to buy bonds of this character. Could all these persons, who were not called as witnesses wilfully and deliberately close their eyes to that which they actually knew? And in the absence of proof that they did not know, how can respondent now successfully claim that it has carried the burden of showing its good faith?

The respondent heretofore has mistakenly relied on the case of *National Bank v. Uptown State Bank, 273 Ill. App. 401.* There it is held that "the evidence does not show specifically that a copy (of the bulletin giving notice of stolen bonds) was mailed to defendant" (p. 405).

Furthermore, and notwithstanding, the Court also held that the defendant was not a holder of the bonds in due course, it having received actual notice that the bonds were stolen while it had the bonds in its possession, and before it had paid out any of the proceeds of the loan. And the Appellate Court definitely shows that cause is entirely different from the instant case by the final paragraph in the decision *(408)*:

> "Finding of fact: We find as a fact that defendant, having in its possession the proceeds of the loan of $3,980, and the four bonds at the time it was notified that the bonds were stolen, is not a holder in due course of the bonds."

The judgment of the United States Circuit Court of Appeals, because of the reasons and errors assigned, should be reversed.

Respectfully submitted,

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APPENDIX.

The Statutes Involved.

United States Code Annotated, Title 28.

Section 347. (Judicial Code, Section 240, amended.) Certiorari to Circuit Court of Appeals and Court of Appeals of District of Columbia; appeal or writ of error to Supreme Court from Circuit Courts of Appeals in certain cases; other reviews not allowed. (a) In any case, civil or criminal, in a Circuit Court of Appeals, or in the Court of Appeals of the District of Columbia, it shall be competent for the Supreme Court of the United States, upon the petition of any party thereto, whether Government or other litigant, to require by certiorari, either before or after a judgment or decree by such lower court, that the cause be certified to the Supreme Court for determination by it with the same power and authority, and with like effect, as if the cause had been brought there by unrestricted writ of error or appeal.

Smith-Hurd Illinois Statutes, Chapter 98, Negotiable Instruments, Article IV.

72. Who is a holder in due course.] §52. A holder in due course is a holder who has taken the instrument under the following conditions:

1. That the instrument is complete and regular upon its face.
2. That he became the holder of it before it was overdue, and without notice that it had been previously dishonored, if such was the fact.
3. That he took it in good faith and for value.
4. That at the time it was negotiated to him he had no notice of any infirmity in the instrument or defect in the title of the person negotiating it.

75. When title is defective.] §55. The title of a person who negotiates an instrument is defective within the meaning of this act when he obtained the instrument, or any signature thereto, by fraud, duress, or force and fear, or other unlawful means, or for an illegal consideration, or when he negotiates it in breach of faith, or under such circumstances as amount to a fraud.

76. Notice of defect—What is.] §56. To constitute notice of an infirmity in the instrument or defect in the title of the person negotiating the same, the person to whom it is negotiated must have had actual knowledge of such facts that his action in taking the instrument amounted to bad faith.

78. When instrument subject to original defenses.] §58. In the hands of any holder other than a holder in due course, a negotiable instrument is subject to the same defenses as if it were non-negotiable. But the holder who derives his title through a holder in due course, and who is not himself a party to any fraud or duress or illegality affecting the instrument, has all the rights of such former holder in respect to all parties prior to such holder.

79. Who is deemed holder in due course.] §59. Every holder is deemed *prima facie* to be a holder in due course; but when it is shown that the title of any person who has negotiated the instrument was defective, the burden is on the holder to prove that he or some person under whom he claims acquired the title as a holder in due course. But the last mentioned rule does not apply in favor of a party who became bound on the instrument prior to the acquisition of such defective title.